

## Message Text

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ACTION EA-10

INFO OCT-01 ISO-00 CIAE-00 DODE-00 PM-03 H-01 INR-07 L-02

NSAE-00 NSC-05 PA-01 RSC-01 PRS-01 SP-02 SS-15

USIA-06 AID-05 EB-07 CIEP-01 TRSE-00 STR-01 OMB-01

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R 171001Z JAN 75

FM AMEMBASSY MANILA

TO SECSTATE WASHDC 9915

INFO AMCONSUL HONG KONG

AMEBASSY BANGKOK

AMEMBASSY CANBERRA

AMEMBASSY JAKARTA

AMEMBASSY KUALA LUMPUR

AMEMBASSY SEOUL

AMEMBASSY SINGAPORE

AMEMBASSY TAIPEI

AMEMBASSY TOKYO

AMEMBASSY WELLINGTON

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E O 11652: N/A

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SUBJ: REVIEW OF PHILIPPINE ECONOMY IN 1974

SUMMARY. THIS MESSAGE REVIEWS THE 1974 PERFORMANCE OF THE PHILIPPINE ECONOMY, IN PART ON THE BASIS OF FIRST CUT YEAR-END DATA. IT WILL BE FOLLOWED BY A MESSAGE ASSESSING THE PROSPECTS FOR THE ECONOMY IN 1975, BUT IT WILL TAKE SOME TIME BEFORE THE DATA BASE FOR THESE APPRAISALS BECOMES VERY FIRM. THE ECONOMY PERFORMED BETTER THAN EXPECTED IN 1974, DESPITE DOMESTIC AND LIMITED OFFICIAL USE

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EXTERNAL INFLATION AND SLOWING DEMAND FOR ITS EXPORTS

IN THE SECOND HALF OF THE YEAR. THE STRONG POINTS OF THE ECONOMY WERE AGRICULTURE AND CONSTRUCTION. ITS WEAKNESSES AROSE SIGNIFICANTLY FROM EXTERNAL DEVELOPMENTS, NOTABLY RISING IMPORT COSTS, REDUCED DEMAND FOR LOGS AND, IN THE SECOND HALF OF THE YEAR WEAKENED MARKETS FOR COPPER CONCENTRATES AND COCONUT OIL. THE GOVERNMENT PRELIMINARILY ESTIMATED ECONOMIC GROWTH AT 5.9 PERCENT AND REPORTED A TRADE DEFICIT OF \$372 MILLION. THE BALANCE OF PAYMENTS SHOWED A SLIGHT SURPLUS WITH HELP FROM THE INVISIBLES SIDE AND WITH MORE THAN \$850 MILLION IN NEW BORROWING. THE RATE OF INFLATION WAS ABOUT 30 PERCENT FOR CALENDAR YEAR, BUT DURING THE LAST SIX MONTHS OF THE YEAR INFLATION DECLINED TO AN ANNUALIZED RATE OF LESS THAN 20 PERCENT. DOMESTIC LIQUIDITY ROSE BY OVER 30 PERCENT. HOWEVER, THE GOVERNMENT SHOWED A SURPLUS OF 2.6 BILLION PESOS. IN CONCLUSION, DESPITE DIFFICULTIES THAT GREW OVER THE YEAR, THE PHILIPPINE ECONOMY LOOKS ON BALANCE TO HAVE PERFORMED BETTER IN 1974 THAN THE ECONOMIES OF MANY OTHER COUNTRIES, A RESULT WHICH HARTENS PHILIPPINE POLICY MAKERS AS THEY LOOK TOWARD FURTHER DIFFICULT CHALLENGES AHEAD. AS IMPORTANT AS THE RESULT ITSELF FROM THEIR VIEWPOINT, HOWEVER, IS APPARENT VINDICATION OF AN OVERALL BALANCE OF PAYMENTS AND DEVELOPMENT STRATEGY WHICH INCLUDED A PATTERN OF EARLY EXTERNAL BORROWINGS AND A WILLINGNESS TO ACCEPT SUBSTANTIAL INFLATION TO ASSURE CONTINUED SIZEABLE INFRASTRUCTURAL INVESTMENT. END SUMMARY.

1. PRODUCTION. THE NATIONAL ECONOMIC AND DEVELOPMENT AUTHORITY HAS REPORTED THAT THE GROSS NATIONAL PRODUCT OF THE PHILIPPINES INCREASED BY 5.9 PERCENT IN 1974. GNP IN CURRENT PRICES WAS REPORTED TO HAVE REACHED 94.8 BILLION PESOS IN 1974, EQUIVALENT TO AN AVERAGE PER CAPITA INCOME OF MORE THAN \$300 AT CURRENT EXCHANGE RATES. WHILE 5.9 PERCENT IS PERHAPS A TOO PRECISE FIGURE AT THIS STATE, IT APPEARS TO US TO INDICATE AN APPROPRIATE RANGE.

(A) THE ECONOMY'S STRONGEST POINT WAS AGRICULTURE, EXPERIENCING SUSTAINED RELATIVELY FAVORABLE PRICES AND LIMITED OFFICIAL USE

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SIZEABLE ABSOLUTE GROWTH IN OUTPUT ESPECIALLY OF RICE. PRODUCTION OF AGRICULTURAL CROPS WAS ESTIMATED BY THE NEDA TO HAVE INCREASED 6.9 PERCENT DURING THE YEAR, AN IMPRESSIVE ACHIEVEMENT FOLLOWING THE RECORD LEVEL OF PRODUCTION IN 1973. ANOTHER BOOST TO THE ECONOMY CAME FROM THE CONSTRUCTION SECTOR WHICH GREW AT 18 PERCENT AND APPEARED TO ACCELERATE TOWARD YEAR'S END AS MATERIAL SUPPLY/PRICE CONDITIONS MODERATED. ON THE NEGATIVE SIDE, PRODUCTION

IN THE LOGGING SECTOR DROPPED 35.6 PERCENT, MINING PRODUCTION INCREASED BY ONLY 0.5 PERCENT AND MANUFACTURING PRODUCTION BY ONLY 3.5 PERCENT. PRODUCTION IN THE TEXTILE INDUSTRY MARKEDLY DECLINED.

(B) THE REPORTED STRENGTH IN AGRICULTURE AND CONSTRUCTION AND THE WEAKNESS IN LOGGING AND MANUFACTURING SHOWED IN THE NEDA REPORTS REFLECTED ADEQUATELY THE OVERALL TRENDS OF THE ECONOMY, EVEN THOUGH THE FIGURES WERE PREPARED BY NEDA ON THE BASIS OF INCOMPLETE DATA. FOR EXAMPLE, CENTRAL BANK INDEXES (WHICH SHOW INCIDENTALLY AN INCREASE IN EMPLOYMENT OF 5.9 PERCENT) REPORT AN INCREASE IN PRODUCTION OF AGRICULTURAL CROPS OF 10 PERCENT AND A DECREASE IN LOGGING PRODUCTION OF ONLY 22 PERCENT.

2. TRADE. THE VALUE OF PHILIPPINE TRADE ROSE SHARPLY IN 1974. THIS SHARP INCREASE WAS MAINLY ATTRIBUTABLE TO PRICE INCREASES AS IMPORT VOLUME ROSE LESS SHARPLY AND EXPORT VOLUME DECLINED. THE DEPARTMENT OF TRADE HAS PROJECTED 1974 EXPORTS OF \$2.8 BILLION AND IMPORTS OF \$3.1 BILLION ON THE BASIS OF PRELIMINARY OCTOBER FIGURES. THE CENTRAL BANK'S PRELIMINARY STATISTICS SHOW EXPORT RECEIPTS OF \$2.5 BILLION AND IMPORT PAYMENTS OF \$2.9 BILLION. THE INCREASE IN EXPORT RECEIPTS OVER 1973 WAS ABOUT 50 PERCENT AND IN IMPORT PAYMENTS NEARLY 100 PERCENT. THE VOLUME OF IMPORTS OTHER THAN PETROLEUM IS ESTIMATED TO HAVE RISEN AS MUCH AS 20 PERCENT. HOWEVER, PRELIMINARY DATA RECENTLY MADE AVAILABLE INDICATE THE VOLUME OF EXPORTS IN 1974 MAY HAVE DECLINED BY AS MUCH AS 24 PERCENT, PRESUMABLY BECAUSE OF DECLINES IN EXPORTS OF LOGS AND COCONUT PRODUCTS.

(A) THE LEADING PHILIPPINE EXPORTS ACCORDING TO LIMITED OFFICIAL USE

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DEPARTMENT OF TRADE SOURCES WERE SUGAR AT \$707 MILLION, COPPER CONCENTRATES AT \$422 MILLION, COCONUT OIL AT \$376 MILLION AND LOGS AND LUMBER AT \$262 MILLION. LEADING IMPORT CATEGORIES WERE MINERALS, FUELS AND LUBRICANTS \$650 AND MACHINERY OTHER THAN ELECTRIC \$410 MILLION.

(B) THE DEPARTMENT OF TRADE FIGURES INDICATE THE U.S. WAS THE PHILIPPINES LEADING MARKET, TAKING NEARLY 45 PERCENT OF ALL PHILIPPINE EXPORTS. THE PHILIPPINE TRADE BALANCE WITH THE U.S. WAS A \$410 MILLION SURPLUS AFTER TEN MONTHS. JAPAN ENJOYED THE LARGEST SHARE OF THE PHILIPPINE MARKET, 28 PERCENT, FOLLOWED BY THE U.S. AT 23 PERCENT. THE PHILIPPINES SHOWED DEFICITS IN ITS ACCOUNTS WITH SAUDI ARABIA, KUWAIT, IRAN AND BAHRAIN.

3. BALANCE OF PAYMENTS. THE CENTRAL BANK'S PRE-LIMINARY PAYMENTS STATISTICS SHOW A TRADE DEFICIT OF OVER \$370 MILLION FOR 1974 AS COMPARED WITH A SURPLUS OF \$293 MILLION FOR 1973, REFLECTING AN ADVERSE SWING OF OVER \$660 MILLION. CURRENT INVISIBLE TRANSACTIONS EXCLUSIVE OF CAPITAL FLOWS ACHIEVED A SURPLUS OF \$456 MILLION GIVING THE COUNTRY A SURPLUS OF MORE THAN \$80 MILLION ON CURRENT ACCOUNT. THE PHILIPPINE INVISIBLE SURPLUS WAS ATTRIBUTABLE TO SHARP INCREASES IN EARNINGS FROM TOURISM, RISING EMIGRANT REMITTANCES AND TRANSFER PAYMENTS UNDER THE U.S. VETERAN'S AND SOCIAL SECURITY PROGRAMS.

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TO SECSTATE WASHDC 9916  
INFO AMCONSUL HONG KONG  
AMEMBASSY BANGKOK  
AMEMBASSY CANBERRA  
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(A) NON-MONETARY CAPITAL INFLOWS AND OUTFLOWS WERE NEARLY BALANCED. THE \$14 MILLION DEFICIT ON THIS ACCOUNT REDUCED THE ECONOMY'S OVERALL SURPLUS TO \$90 MILLION. THE COUNTRY'S GROSS RESERVES ROSE \$274 MILLION TO \$1,152 MILLION OF WHICH \$204 MILLION WAS ATTRIBUTED TO COMPENSATORY BORROWINGS BY THE CENTRAL BANK. NET RESERVES (GROSS RESERVES MINUS LIABILITIES OF COMMERCIAL BANKS AND SHORT-TERM LIABILITIES OF CENTRAL BANK) DECLINED, HOWEVER, BY ABOUT \$50 MILLION TO A ROUGH YEAR END TOTAL OF \$600 MILLION, AS COMPARED WITH \$650 MILLION IN LIMITED OFFICIAL USE

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NET RESERVES AT THE END OF 1973.

4. EXTERNAL DEBT. A MAJOR INCREASE IN PHILIPPINE EXTERNAL DEBT CONTRIBUTED AN ESTIMATED 1974 BALANCE OF PAYMENTS SURPLUS OF OVER \$90 MILLION.

EXTERNAL DEBT OUTSTANDING AT YEAR'S END HAD RISEN BY ONE-THIRD FROM \$2.4 BILLION AT THE BEGINNING OF 1974 TO \$3.2 BILLION. NEW BORROWINGS INCLUDED \$410 MILLION BY THE CENTRAL BANK, \$204 MILLION OF WHICH WAS IDENTIFIED AS COMPENSATORY BORROWINGS. THE BULK OF BORROWINGS BY THE PRIVATE SECTOR WERE IN SHORT-TERM REVOLVING CREDITS. NEVERTHELESS, ENOUGH MEDIUM AND LONG-TERM BORROWING OCCURRED TO PREVENT A SHARP DROP IN NET RESERVE LEVELS.

(A) THE NEW BORROWINGS WILL INCREASE THE COUNTRY'S DEBT SERVICE BURDEN, BUT THE IMPACT OF THIS INCREASE WILL BE TEMPERED BY THE RISE IN THE ECONOMY'S DEBT SERVICE CAPABILITY. THE RAPID RISE IN CURRENT RECEIPTS IN 1974 WILL LOWER THE RATION OF SERVICE PAYMENTS ON MEDIUM AND LONG-TERM DEBT TO CURRENT RECEIPTS FROM THE 20 PERCENT FIGURE PREVAILING AT THE END OF 1973. HOWEVER, THE BURDEN OF SHORT-TERM DEBT HAS ALSO INCREASED ALTHOUGH THE EXTENT AND IMPACT OF THIS INCREASE IS NOT CLEAR. ACCORDING TO CENTRAL BANK STATISTICS REVOLVING CREDITS ACCOUNTED FOR 65 PERCENT OF THE COUNTRY'S INCREASE IN DEBT DURING 1974. AN INCREASED PAYMENT LEVEL WILL BE NECESSARY TO SERVICE THE GROWING VOLUME OF REVOLVING CREDIT.

5. INFLATION. THE PHILIPPINE ECONOMY CONTINUED TO SUFFER FROM RAPID INFLATION DURING THE FIRST HALF OF 1974, BUT THE RATE SLOWED MARKEDLY IN THE

SECOND HALF. STATISTICS RELEASED BY GOVERNMENT AGENCIES INDICATED THAT IN 1974 PHILIPPINE PRICES INCREASED ABOUT 30 PERCENT. THE NEDA REPORTED A GROWTH RATE FOR THE GROSS NATIONAL PRODUCT IN CURRENT PRICES OF 36.3 PERCENT, AS COMPARED WITH A 5.9 PERCENT GROWTH REPORTED IN CONSTANT 1967 PRICES. THE CENTRAL LIMITED OFFICIAL USE

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BANK REPORTED THAT CONSUMER PRICES IN MANILA WERE 27.2 PERCENT HIGHER IN DECEMBER OF 1974 THAN THEY HAD BEEN IN DECEMBER OF 1973....

(A) THE FUEL-LIGHT-WATER COMPONENT OF THE CONSUMER PRICE INDEX GREW MOST RAPIDLY (98 PERCENT) REFLECTING THE SEVERAL FOLD INCREASE IN PETROLEUM PRICES. CLOTHING PRICES WENT UP 45 PERCENT. FOOD PRICES ROSE 39 PERCENT AND WERE A MAJOR FACTOR IN THE OVERALL RISE IN CONSUMER PRICES. THE RISE IN FOOD PRICES WAS BROADLY BASED. CEREAL PRICES ROSE 38 PERCENT, FISH PRICES 43 PERCENT AND FRUIT AND VEGETABLE PRICES 52 PERCENT. INFLATION PEAKED IN THE FIRST HALF OF THE YEAR AND SLOWED IN THE SECOND. THE MANILA CONSUMER PRICE INDEX, FOR EXAMPLE, ROSE 35 PERCENT ON AN ANNUAL BASIS FROM JANUARY TO JUNE BUT ONLY 16.6 PERCENT ON THE SAME BASIS FROM JULY TO DECEMBER.

6. FINANCIAL POLICIES. CHANGES IN PHILIPPINE FINANCIAL POLICIES IN 1974 INCLUDED THE DEPRECIATION OF THE PESO BY SLIGHTLY MORE THAN 4 PERCENT, A 21 PERCENT INCREASE IN THE MONEY SUPPLY, A SURPLUS OF PESO 2.6 BILLION IN THE GOVERNMENT'S CURRENT OPERATIONS AND AN EFFORT BY THE GOVERNMENT TO REDIRECT CREDIT, MAINLY TO AGRICULTURE. THE DEPRECIATION OF THE PESO IN NOVEMBER REDUCED ITS VALUE TO \$1.00-PESO 7.067, FROM THE PESO 6.67 RATE ESTABLISHED BY FLOAT IN 1972. TOTAL LIQUIDITY IN THE ECONOMY GREW BY 31 PERCENT OVER THE YEAR TO PESO 25 BILLION. TOTAL CREDITS INCREASED 35 PERCENT TO PESO 25.5 BILLION OF WHICH PRIVATE SECTOR CREDITS ACCOUNTED FOR PESO 24 BILLION. GOVERNMENT EXPENDITURES ROSE TO PESO 14.6 BILLION PESOS AND RECEIPTS TO PESO 17.2 BILLION OF WHICH PESO 579 MILLION REPRESENTED NET BORROWINGS. THE GOVERNMENT'S CASH POSITION AT YEAR END WAS NEARLY PESO 7.0 BILLION. OUTSTANDING CENTRAL BANK CERTIFICATES OF INDEBTEDNESS AT YEAR END TOTALLED PESO 3.4 BILLION OF WHICH PESO 1.6 BILLION HAD BEEN CHanneled TO FOOD AND EXPORT PRODUCTION.

7. GENERAL COMMENT. SEVERAL FEATURES OF THE YEAR'S PERFORMANCE DESERVE SPECIAL NOTE IN THIS FIRST CUT LIMITED OFFICIAL USE

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APPRAISAL. FIRST, THE COUNTRY ENTERED THE YEAR IN SOME SHOCK AND CONFUSION ABOUT BALANCE OF PAYMENTS AND GROWTH CONSEQUENCES OF ENERGY PRICE CHANGES. WHILE THIS WAS HARDLY UNIQUE, THE FILIPINOS BOTH SAW AND WORKED TO COVER THEIR EXTERNAL FINANCIAL NEEDS WELL AHEAD OF MANY OTHERS. THOSE BORROWINGS CONTRIBUTED TO A HIGH, SIGNIFICANTLY COSMETIC YEAR-END RESERVE POSITION. LEADERSHIP ALSO BIT THE BULLET BY LETTING CONSUMER PRICES OF OIL PRODUCTS AND ENERGY MOVE UP SEVERAL FOLD, BEGINNING THE YEAR WITH ITS LARGEST AND LUMPIEST COMPONENT OF INFLATION TO ABSORB ALMOST IMMEDIATELY. A CONSCIOUS CHOICE WAS MADE TO RIDE THIS OUT AND PERHAPS TO EXACERBATE THE INFLATION RATE BY CONTINUEUD DEVELOPMENT SPENDING, ESPECIALLY ON INFRASTRUCTURE, AND BY CREDIT EXPANSION, WITH AGRICULTURE AS A SPECIAL TARGET. HOWEVER, A NUMBER OF FACTORS, INCLUDING DIFFICULTIES IN LAUNCHING NEW PROJECTS, SIZEABLE NET BORROWINGS OF THE CENTRAL BANK AND A SECOND YEAR OF GROWTH IN REVENUE COLLECTIONS WHICH YIELDED A BUDGET SURPLUS, COLLECTIVELY RESULTED IN AN OVERALL CONTRACTIONARY IMPACT OF GOVERNMENT ACTIVITIES. STEPS ALSO WER TAKEN EARLY IN THE YEAR TO CURB HIGH EXPORT PROFITS AND INCREASE THE GOVERNMENT ROLE IN COMMODITY TRADE. THESE STEPS, EXCEPT FOR SUGAR MARKETING, FACED REVIEW AS THE YEAR PROGRESSED AND EXPORT PRICES WEAKENED. THE WEAKEST AREAS OF PERFORMANCE LAY IN EFFORTS TO REDUCE UNEMPLOYMENT AND TO BOLSTER LAGGING EXPORT ACTIVITIES. THE MOST IMPRESSIVE SECTOR RESULT, DESPITE 23 TYPHOONS IN 1974, WAS IN AGRICULTURE. WHILE THE FINAL RESULT MAY TAKE SOME TIME TO TABULATE, A DEFENSIVE BALANCE OF PAYMENTS STRATEGY WITH A DOMESTIC EMPHASIS ON FURTHER DEVELOPMENT AND EXPANSION OF PUBLIC INFRASTRUCTURE APPEARS TO HAVE PAID OFF, ABOUT AS MUCH AS ONE SHOULD EXPECT IN THE INCREASINGLY UNCERTAIN WORLD ECONOMIC SETTING.

SULLIVAN

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